Before the

FEDERAL COMMUNICATIONS COMMISSION

Washington, D.C. 20554

In the Matter of:

TABLE OF CONTENTS

SUMMARY i

I. A SIMPLIFIED SYSTEM OF REGULATION SHOULD APPLY TO SYSTEMS WITH LESS THAN 1,000 SUBSCRIBERS. 2

A. A Different System of Regulation Is Warranted for Small Systems 2

1. Congress Specifically Directed the FCC to Reduce Administrative Burdens on Small Systems 2

2. Regulatory Burdens Fall Disproportionately On Small Systems 3

3. Small Systems Have Higher Costs Than Large Systems, And Therefore Require A More Flexible Regulatory Scheme 5

B. Neither the Commission's Benchmark Scheme of Regulation Nor the Actual Benchmarks Are Appropriate for Application to Small Systems 6

C. Only Those Small Systems With Net Income In Excess Of A Certain Percentage Of Gross Revenues Should Be Required To Undertake A Benchmark Analysis, And Benchmarks Should Be Adjusted Upward Where Density Is Low. 10

1. Small Systems With "Reasonable Net Income" Should be Deemed to Have Reasonable Rates. 12

2. Small Systems Whose Net Income Exceeds "Reasonable Net Income" Should Evaluate Their

c. Equipment Prices should not be Separately Regulated for Small Systems. 16

d. Systems Should Be Permitted To Pass Through Increases In Costs Since September 30, 1992. 17

3. Streamlined Cost-of-Service Analysis Should Be Permitted for Small Systems 18

III. THE FCC SHOULD PERMIT MORE PASS-THROUGHS FOR EXOGENOUS COSTS 19

IV. IT IS IMPERMISSIBLE FOR THE FCC TO THREATEN TO PUNISH SYSTEMS SEEKING TO JUSTIFY RATES BASED ON COST-OF-SERVICE PROCEDURES. 21

CONCLUSION 22

SUMMARY

The Coalition of Small System Operators requests reconsideration of the Rate Regulation Report and Order. The Coalition consists of 24 cable operators serving about 1.25 million subscribers from almost 25 percent of the nation's headends. The average system operated by the Coalition serves 335 subscribers.

The Coalition believes that the Commission has failed to meet its statutory mandate to design rate regulations that "reduce the administrative burdens and cost of compliance" for cable systems serving less than 1,000 subscribers. To the contrary, the benchmark system created by the Rules adopted on April 1, 1993, are incredibly complex and require time-consuming and complicated analyses for every individual system. Instead of designing regulations that are less burdensome for small systems, the Commission has designed regulations that are the most burdensome on small systems. The small systems, by definition, have the fewest subscribers (and staff, etc.) per system. Yet the rules require the same analysis to be performed for every system, regardless of its size. Some of the Coalition members have been burdened with requirements that they compute hundreds of benchmarks and thousands of equipment prices. Many small systems simply have been unable to complete the analyses. And under the statute, they should not have to.

The benchmarks developed by the Commission for small systems rely heavily on the prices charged by cable systems engaged in below-cost price wars and by municipally-owned cable systems that do not have the same cost (and profit) requirements as private systems. William Shew of Arthur Andersen Economic Consultants has determined that the systems in the FCC's database that have been engaged in head-to-head competition for five years or less have prices fully 25 percent below systems where such competition has been sustained

more than five years. This statistically significant difference proves what everyone with any knowledge of cable overbuilds intuitively or empirically understands -- the early years of overbuild competition are marked by price wars where prices do not cover longrun average costs. It is unquestionably arbitrary and capricious for the Commission to suggest that prices charged by cable systems which are not in competitive equilibrium should be the model for prices in perfect competition.

In addition, Mr. Shew finds that the prices charged by municipal systems -- which have access to cheaper financing (tax exempt bonds), free use of public rights of way, and exemptions from franchise fees and property taxes, and which do not have equity investors who need to make a profit -- are 15 percent lower even than the prices charged by competing private systems. Again, it is arbitrary and capricious to base rates for private "non-competitive" cable systems on the prices charged by municipal systems.

The illogic of the benchmark system as constructed by the FCC is highlighted by the fact that 20 of the 45 competitive small systems used by the FCC in setting the benchmarks themselves charge prices above the benchmarks. Indeed, these 20 systems exceed the Commission's benchmarks by an average of 26 percent. Yet these competitive systems do not have to reduce their prices to the level required for non-competitive systems.

which do not exceed that net income, as a percentage of revenues, should be deemed to have reasonable rates. Moreover, the analysis should be permitted to be made on the basis of consolidated accounting systems in place as of April 1, 1993, where the system at issue, and the average system in the consolidated accounting group, have 1,000 subscribers or less.

Where the system has net income in excess of this percentage -- either because it has amortization of intangibles (not included in the net income analysis), because it has largely depreciated its plant, or because it has not used debt financing heavily -- the system should be permitted to rely on benchmarks developed without consideration of the competitive systems that do not reflect longrun competitive prices. Although the benchmark system has other deficiencies, we believe it may be used as a second-level analysis of reasonable

unbundle equipment that is not currently the subject of a separate charge. The procedure for doing so is very complex and burdensome, and there is no overall benefit to subscribers. Also, small systems must be permitted to pass through inflation and exogenous cost increases since September 1992, and the types of exogenous costs that may be passed through should be expanded.

In their various recent public statements, the Commissioners have appeared to recognize the enormous unfairness the FCC's rate regulations visit on small system operators. We respectfully request the Commission to reduce that unfairness as suggested in this Petition.

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In the Matter of	)	
	)	
Implementation of Sections of	)	
the Cable Television Consumer	)	MM Docket 92-266
Protection and Competition Act	)	
of 1992	)	
	)	
Rate Regulation	)	

To: The Commission

COALITION OF SMALL SYSTEM OPERATORS PETITION FOR RECONSIDERATION

On behalf of the Coalition of Small System Operators, 1/ we hereby petition for reconsideration of the Commission's rate regulations, as promulgated in *Report and Order and Further Notice of Proposed Rulemaking,* FCC 93-177 (released May 3, 1993) (the "*Rate Report and Order*"). The Small System Operators operate cable television systems primarily serving small, rural communities with very few homes per mile. Together, the Small System Operators operate from more than 2,793 headends, representing almost a quarter of the headends in the

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1/ The Coalition of Small System Operators consists of: ACI Management, Inc.; Balkin Cable; Buford Television, Inc.; Classic Cable; Community Communications Co.; Douglas Communications Corp. II; Fanch Communications, Inc.; Frederick Cablevision, Inc.; Galaxy Cablevision; Harmon Communications Corp.; Horizon Cablevision, Inc.; Leonard Communications, Inc.; MidAmerican Cablesystems, Limited Partnership; MidContinent Media, Inc.; Mission Cable Company, L.P.; MW1 Cablesystems, Inc.; Phoenix Cable, Inc.; Rigel Communications, Inc.; Schurz Communications, Inc.; Star Cable Associates; Triax Communications Co.; USA Cablesystems, Inc.; Vantage Cable Associates; and Western Cabled Systems.

country. 2/ They serve approximately 1,297,856 subscribers. The vast majority of these systems serve less than 1,000 subscribers, with the average system in this group serving approximately 347 subscribers. The average density for these systems is 25 subscribers per mile, as compared with the average number of 37.75 subscribers per mile among the systems in the FCC's rate survey. As illustrated by these numbers, these small systems operate in an entirely different arena than large, metropolitan cable systems, a fact that should be acknowledged by the Commission by the development of rules appropriate for the unique operations of small systems.

I. A SIMPLIFIED SYSTEM OF REGULATION SHOULD APPLY TO SYSTEMS WITH LESS THAN 1,000 SUBSCRIBERS.

A. A Different System of Regulation Is Warranted for Small Systems

1. Congress Specifically Directed the FCC to Reduce Administrative Burdens on Small Systems

Congress recognized the differences in the operations of small and large systems, and expressly provided for the reduction of administrative burdens on small systems -- systems with less than 1,000 subscribers.

> In developing and prescribing regulations pursuant to this section [623], the Commission shall design such regulations to reduce the administrative burdens and cost of compliance for cable systems that have 1,000 or fewer subscribers. 3/

In view of Congress' broad directive, the Commission is required to craft a different set of rules geared toward minimization of administrative burdens

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2/ There are an estimated 56,551,610 basic cable households in the United States and 11,457 headends according to an A.C. Nielsen Study. "Cable Television Development," National Cable Television Association (October 1992).

3/ Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, § 623(i), 106 Stat. 1460 (1992) (the "1992 Cable Act").

on small systems. The Supreme Court has recently upheld the Commission's differential treatment of systems based on the number of subscribers served, recognizing that system size is a characteristic that can rationally distinguish "those systems for which the costs of regulation would outweigh the benefits to consumers." *Federal Communications Commission v. Beach Communications, Inc.*, Slip Op., No. 92-603 (June 1, 1993).

The concern that small system regulation not be administratively burdensome has been reflected in correspondence from members of Congress. For example, the South Dakota Congressional Delegation has requested the Commission to "take into account the special danger of excessive administrative burdens on . . . small systems." *See* Letter to Chairman Quello from Senators Tom Daschle and Larry Pressler, and Congressman Tim Johnson, March 5, 1993, attached hereto as Exhibit 1. Chairman Quello's response to the South Dakota Delegation noted that the FCC's rate regulation proceeding "specifically seeks comment on ways to reduce the burdens on small cable systems." *See* Letter to Senator Tom Daschle, from Chairman Quello, March 29, 1993, attached hereto as Exhibit 2.

We respectfully submit that the Commission's rules do not adequately reduce the burdens on small cable systems. In fact, the burdens of the rules on small systems are crushing. The Commission should -- and we believe must, under the statute -- now act decisively to amend its rules to reduce those burdens.

2. Regulatory Burdens Fall Disproportionately On Small Systems

The Commission's regulatory program as adopted on April 1, 1993, imposes enormous administrative and financial burdens on small system operators. These operators are currently shouldering exorbitant administrative costs in an effort to comply with the many new rules promulgated under the 1992 Cable Act,

regulating all facets of their operations. One Small System Operator (with an average of 462 subscribers per system) sent out 1,259 letters to broadcasters by the May 3, 1993 deadline under the new signal carriage rules. The same operator sent out 2,271 signal carriage notifications to broadcasters on June 1, 1993. And, since May, it has responded to 375 inquiries from broadcasters asking for clarification of additional information relating to signal carriage. The operator expects to engage in more than 100 sets of retransmission consent negotiations by October 1993. *See* Declaration of Dean Wandry, Exhibit 3. These examples illustrate the enormous administrative burdens that can accompany regulations and their disproportionate effect on small operators. We note also that these examples represent only a few of the requirements of the signal carriage rules, let alone the many other areas that have been recently regulated, such as the new rigorous customer service standards applicable across the board to all sizes of systems, technical rules, home wiring rules, anti-trafficking rules, anti-buy-through rules, and indecency/obscenity rules.

Before the Commission granted a stay of the rate regulations, Small System Operators were required to spend a huge amount of time, and to devote substantial portions of their operating budgets to their efforts to digest and implement the rate regulations, complete the worksheets, and develop compliance strategies. We remind the Commission that it took a staff member almost one hour to explain how to fill out the worksheets, even without having to obtain the information to be included. Because calculations are required on a system-by-system basis, some Coalition members were required to complete hundreds of worksheets to determine benchmark compliance, and to complete literally thousands of equipment price computations. The average Small System Operator in the Coalition was required to fill out the worksheets for each of 219 systems. Personnel who would otherwise have been charged with handling other vital financial and administrative duties for the Small System Operators were diverted

to the sole task of completing worksheets and calculating benchmarks for their franchises by June 21, 1993. Even with this substantial dedication of resources, many of the Small System Operators were finding it impossible to complete calculation of the benchmarks with any level of certainty because of the complexity of the issues, the huge number of franchises served by the Small System Operators (the average number of community units served by each of the Small System Operators is 219), and the time constraints. *See* Declaration of Michael J. Pohl, Exhibit 4; Declaration of Dean Wandry, Exhibit 3. Although cable operators have now been given a reprieve with respect to the timing of the implementation of rate regulation, the complexity and administrative burdens imposed by the benchmark system of regulations have not yet been addressed.

3. Small Systems Have Higher Costs Than Large Systems, And Therefore Require A More Flexible Regulatory Scheme

The configuration of small systems is such that per subscriber costs are substantially higher than for larger systems. Administrative costs, per subscriber, for example, are significantly higher for small systems. One Small System Operator estimates that, even before passage of the 1992 Cable Act, it was required to prepare and file approximately 4,250 separate reports each year with government entities for its 416 systems, which served about 304,734 subscribers. This amounts to one report for every 72 subscribers. By contrast, a larger operator with a single system of 304,000 subscribers would have to make only about 10 annual filings, or one report for 29,803 subscribers.

The Small System Operators must also deal with many more franchise authorities than large operators, adding to their administrative costs. One typical Small System Operator has approximately 200 franchises serving a total of about 52,335 subscribers (an average of 261 subscribers per franchise). The costs of

negotiating, tracking and insuring compliance with these various agreements are substantial, especially when compared with the cost of a single franchise agreement required for a given metropolitan area system serving a large number of subscribers.

Programming is another area in which small systems have disproportionately high costs. It is well known that small systems have higher costs for programming than larger systems, as small systems generally do not qualify for volume discounts on programming. The premium prices that small operators must pay for programming must be recovered from subscribers.

To add to the problems posed by these high costs incurred by small systems, the revenue streams for small systems are also more limited than those of large operators, and therefore it is more difficult for small systems to recover these disproportionate administrative costs. For example, small operators generally do not have the technical ability to insert local advertising; they often do not have the technical ability to offer pay-per-view services; and even the number of channels that may be offered is more limited due to technical and cost considerations. Therefore, these operators rely much more heavily on their revenues from regulated services than revenues from unregulated services to cover their substantial per-subscriber costs.

B. Neither the Commission's Benchmark Scheme of Regulation Nor the Actual Benchmarks Are Appropriate for Application to Small Systems

In establishing its rate benchmarks, the Commission relied on data from surveys, as described in Appendix E to the *Rate Regulation Report and Order*. The survey form sought only information regarding prices, and not costs. Of the 1107 community units for which responses were received, the Commission determined that the 141 of them operating in competitive environments should

serve as the primary basis for the benchmarks. Of these 141 systems, 79 were systems with less than 30 percent penetration, 46 faced actual competition, and 16 were found to be competitive as municipal overbuilds or municipal systems. Only 45 of the 141 systems found to operate in competitive environments were systems with less than 1,000 subscribers. Of these, 32 had less than 30 percent penetration, 7 were found to face actual competition, and 6 were municipal systems.

As explained in the attached Declaration of William Shew, Director of Arthur Andersen Economic Consultants, "[e]ven the figure of 45 almost certainly overstates the number of cable systems in the database capable of providing a reliable guide to 'competitive' prices," Exhibit 5 at 11. This is because "[m]arkets involving municipal cable systems and short-term overbuilds cannot be expected to provide a reliable guide to the prices that characterize sustainable competition between private cable systems." *Id.* at 12.

For example, of the seven private small systems in the survey found to be facing actual competition, six had existed for five years or less. "Such short-term competition is typically characterized by price wars, during which prices are often held well below average total cost." *Id.* at 11. Therefore, as explained more fully in the Declaration of William Shew, it is likely that the systems facing actual competition are operating at or below cost in an effort to gain a competitive edge in the short run. Significantly, the Commission has made no effort to determine whether any of these systems facing actual competition are operating at a profit, or realizing a reasonable return on investment. As explained by Mr. Shew, we would expect to find that systems involved in the initial years of direct competition are charging prices that would not sustain long-term operations. And, not surprisingly, "in franchises where the duration of competition was five years or less, prices were 25% less than in those franchises where competition had endured more than five years." *Id.* at 14. This is a statistically reliable indication that these systems are

pricing themselves below longrun average costs. Nevertheless, the Commission has relied on these systems in setting its benchmarks -- as if the fact that two adjacent gas stations are charging 20 cents a gallon while engaged in cut throat competition means that 20 cents should be taken as the "competitive price." The Commission's reliance on systems which have been engaged in head-to-head competition for five years or less to determine the benchmarks for rates is at odds with the statutory command that the Commission should develop reasonable rates.

In addition, municipal systems have significant cost advantages over private systems. An analysis of the municipal systems in the FCC database demonstrates that "basic service prices charged by municipal systems are almost 15% below prices charged by competing private systems, other factors equal." *Id.* at 12 (emphasis added). Therefore, municipal systems are even less reliable than private systems in head-to-head competition as predictors of longrun competitive rates.

Not only are there flaws in the data used to develop the benchmarks, but the methodology also is illogical, as illustrated by the fact that the benchmarks require non-competitive systems to charge prices below the prices charged by many of the competitive systems that provided the basis for the benchmarks. As explained in Mr. Shew's Declaration, 20 of the 45 small systems found to be competitive by the FCC are charging rates **above** the benchmarks. *Id.* at 18. On average, these systems' rates exceeded the prices predicted by the Commission's equation by 26 percent. *Id.* However, these systems will not be required to reduce their rates because they are not subject to rate regulation under the Cable Act. Thus, small, non-competitive systems will be required to charge lower rates under the benchmarks than the competitive systems whose rates provided the basis for the benchmarks. This result is utterly irrational.

The real-life results of the FCC's flawed benchmarks could mean loss of service to subscribers. According to one of the Small System Operators, which was asked by creditors to turn around and manage eight systems in financial trouble, the progress it has made in decreasing the systems' net losses would be completely undermined by application of the benchmarks to the systems' rates. Reduction of rates to the benchmarks would result in violation of credit documents and ultimately could lead to bankruptcy and deactivation of the systems, which serve approximately 2,000 subscribers in rural areas. *See* Declaration of Vince King, Exhibit 6.

Another Small System Operator reports that reduction to the level required by the benchmarks would increase its current net losses "to the point where revenues would not cover all of the current interest expense associated with the system, excluding (non-cash) depreciation and amortization charges." *See* Declaration of Jay Busch, Exhibit 7. If this occurred, the operator would have to consider as an alternative ceasing operations in the system. *Id.*

A Small System Operator with 460 franchise areas that would each require a separate benchmark analysis under the FCC's rules estimates that reduction of rates to the benchmark level would have produced a net loss of $9,346 over the past 12-month period, and projects that the same system would experience a net loss of $7,838 over the next 12 months. This operator, like others, is wary of the threat that rates could be reduced to below-benchmark levels, and therefore would hesitate to rely on the cost-of-service alternative. *See* Declaration of Dean Wandry, Exhibit 2.

For Small System Operators, the procedures implementing the Commission's benchmark rates are as irrational as the benchmarks themselves. The franchise-by-franchise analysis of rates may not unduly burden metropolitan systems serving one or two franchise areas from a single headend. By stark

contrast, one of the Small System Operators with approximately 468 franchises, almost all of which serve less than 1,000 subscribers, with an average of 217 subscribers per franchise area, is inundated with worksheet forms at an exorbitant per subscriber administrative cost. *See* Declaration of Michael J. Pohl, Exhibit 4. It does not make sense to impose the across-the-board requirement that systems complete the bevy of worksheets (and related forms), particularly for a system that is operating with net loss or an incontrovertibly reasonable net income. These systems with high costs and net losses (or limited net income) clearly cannot afford to reduce their rates, rendering moot the onerous exercise of completing the many worksheets. Similarly, cost-of-service procedures are too complicated and costly to undertake for small systems with tight operating margins. The streamlined approach set forth below would, consistent with Congress' directive, reduce the administrative burdens on those small systems who can least afford to undertake a complicated, lengthy compliance analysis.

C. Only Those Small Systems With Net Income In Excess Of A

the system's rates would be deemed per se reasonable, with no further analysis required. 4/

If the system's net income exceeds a per se reasonable percentage of gross revenues, the system would be required to undertake either a benchmark analysis or a cost-of-service analysis. Although we believe the benchmark analysis leaves much to be desired, benchmarks provide an acceptable indication of "reasonable rates" under the statute where they are not based on the rates charged by municipal or short-term competitive systems, and where they are subject to certain adjustments designed to take into account the higher costs faced by operators in areas with low subscriber density. In addition, where both the particular system and the average system in an operator's consolidated accounting group contain less than 1,000 subscribers, the operator should be allowed to rely on its consolidated numbers.

If the system's regulated rates exceed the benchmark, as appropriately adjusted, then the system would have the option to proceed to the third step in the regulatory analysis, preparation of a cost-of-service analysis. This three-level

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4/ We believe that few would argue that systems with a net loss have unreasonable rates. But we also believe that all would agree that cable systems are entitled to net income that comprises at least some minimal percentage of revenues. The Coalition of Small System Operators is undertaking to determine what percentage of gross revenues would constitute a per se reasonable amount of net income. However, because of the many other pressing issues that the Coalition has addressed during the last several weeks (*e.g.* Petition for Stay of Rate Regulation Rules filed June 11, 1993; Comments on Further Notice of Proposed Rulemaking with respect to rate regulation filed June 17, 1993; examination of cost-of-service procedures in an effort to develop streamlined procedures to propose to the FCC), the Coalition has not been able to complete the research regarding a percentage of gross revenues that would be unquestionably accepted as reasonable. That percentage will be supplied to the Commission in a supplemental filing. For purposes of this filing, we will refer to situations where systems' net income is below this certain percentage of gross revenues as systems with "**Reasonable Net Income**."

regulatory structure would properly reduce the administrative burdens on those small systems already operating with reasonable profits (or losses), while retaining the general principles and procedures of the benchmark/cost-of-service regulations.

1. Small Systems With "Reasonable Net Income" Should be Deemed to Have Reasonable Rates.

As a first step, we believe that an operator with a consolidated accounting system in place on April 5, 1993 (with an average system size of less than 1,000 subscribers) should be allowed to rely on that accounting system to

We believe that there cannot be any serious question that small systems earning less than a certain, incontrovertibly reasonable percentage of gross revenues after subtracting operating expenses, depreciation, and interest expense are charging reasonable rates. The calculation is, in essence, a primitive form of cost-of-service analysis. It avoids the potential controversial issues of allocation between regulated and unregulated services by including all revenues generated by the systems, except extraordinary items such as sale of a portion of the system. It includes operating expenses and depreciation, as it must, but it excludes amortization of intangibles, again to avoid controversy. Finally, it includes interest expense, an expense that must be met in order for the system to survive economically. Certainly, if the system has negative net income under this calculation, we believe all would agree that its rates must be deemed reasonable overall. But the reasonableness of its rates may also be proven where the system's net income is no more than a certain percentage of its gross revenues.

The Coalition believes that the 1992 Cable Act requires the FCC to create a threshold analytical framework for small systems' rates that is much simpler and with less administrative costs than the benchmark system contained in the rules adopted April 1, 1993. The simplified net income analysis we propose here would allow small system operators, on the basis of their existing accounting systems, to quickly and easily determine whether their rates are reasonable. The completed one-page form we propose could be supplied to the local regulating authority or to the FCC in response to a complaint to justify current rates where appropriate. And where small systems are making more than a certain percentage of gross revenues as net income, those rates may nevertheless be justified by use of the more complex methods available to all cable operators.

2. Small Systems Whose Net Income Exceeds "Reasonable Net Income" Should Evaluate Their Rates Using A Revised Benchmark Formula.

a. Benchmark Tables Governing Systems With Less Than 1,000 Subscribers Should be Revised.

Some small systems may be charging "reasonable" rates, even if they do not meet the standard set by the net-income analysis. For example, they may have amortization of intangibles that properly should be permitted. They may have largely depreciated plant. Or they may have a large percentage of equity financing so that they do not rely heavily on debt. The Coalition believes that where small systems do not meet the net income test, they should be permitted to rely on revised

b. The Benchmarks For Small Systems Should Be Adjusted Upward For Low Density.

As demonstrated by the table and graph attached to the Declaration of Tony Kern, Exhibit 9, the per subscriber cost of construction for systems in low density (measured in subscribers per mile) areas is substantially higher than for systems in more densely populated areas. The per subscriber construction costs gradually increase as density decreases from the average of 37.75 subscribers per mile, 6/ until density reaches about 30 subscribers per mile, at which point the increases in per subscriber costs begin to rise dramatically. *See id.* Based on a conservative cost per mile of construction of $15,000 and straight-line depreciation over 12 years, 7/ the monthly depreciation for cable distribution plant per subscriber is $2.76 for systems with 37.75 subscribers per mile (representing the average of the FCC's database); $2.98 for systems with 35 subscribers per mile; $3.47 for systems with 30 subscribers per mile; $4.17 for systems with 25 subscribers per mile; and $5.21 for systems with 20 subscribers per mile. *Id.* Based on the dramatic increases in per subscriber costs at the density of 30 subscribers per mile, the Commission should permit small systems with less than 30 subscribers per mile to adjust their benchmark rates by the specific amounts contained in Mr. Kern's declaration to account for the extra per subscriber construction costs.

The actual number by which the benchmarks should be adjusted for a given system may be reached, as discussed above, by assuming straight-line depreciation over twelve years and construction costs of 15,000 per mile of

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6/ This is the average number of subscribers per mile for the systems in the FCC survey database. *See* Declaration of Tony Kern, Exhibit 9.

7/ It is conservative to assume an average construction cost of $15,000 per mile of plant and to depreciate plant over 12 years. *See id.*

distribution plant. Under these conservative assumptions, a system serving 12 subscribers per mile 8/ would have to recover $104.00 annually per mile of plant ($8.68 per month from each subscriber) in order to cover the depreciation for these construction costs, while, all other factors being equal, a system with density of 37.5 subscribers per mile would have to recover only $2.76 per month from each subscriber to cover depreciation. Therefore, even completely ignoring the fact that other non-subscriber costs are also higher for systems with low density (see

require that the prices charged by small systems for equipment be based on costs where the regulations would be administratively burdensome.

The additional burden of completing the FCC worksheets required for the calculation of equipment costs and unbundling impact unfairly on small systems who have neither the in-house personnel nor the resources to hire outside consultants to prepare the many forms required for the equipment analysis. Moreover, there will be no meaningful differences in rates based on the elaborate procedures, and equipment prices will remain regulated in any event based on their inclusion in regulated programming rates. The burden of making small systems undergo a separate analysis for regulated programming rates and equipment rates simply outweighs any benefit of requiring such an analysis, and the benefit to consumers is illusory.

Requiring that equipment prices be revised according to the FCC's complicated worksheets also creates a likelihood that, even where small systems' overall rates remain the same, the prices for subscribers taking a minimum of equipment will rise, while subscribers taking a maximum amount of equipment (such as remotes and additional outlets) will see a rate decrease. Not only will this cause unnecessary and complicated rate adjustments but there will be no overall benefit to small system subscribers. We respectfully request that small system

September 30, 1992 levels), the system should be permitted to adjust its rates after the freeze period in order to compensate not only for inflation but also for increases in other exogenous costs since September 30, 1992.

The Commission's price-cap system allows systems with rates above the benchmarks to adjust the benchmarks upwards (toward existing prices) based on inflation from September 30, 1992, to the date of regulation. But the Commission does not permit these systems to adjust for increases in exogenous costs during that period. Because the Commission recognizes the reasonableness of adjusting for exogenous costs after regulation begins, it is wholly irrational not to recognize increases in these costs since September 30, 1992.

Moreover, the price-cap system does not permit cable operators whose rates are currently below the benchmarks to adjust their rates at all for either inflation or exogenous cost increases occurring between September 30, 1992, and the date of regulation. Plainly, this is irrational and unfairly penalizes those systems with low rates.

3. Streamlined Cost-of-Service Analysis Should Be Permitted for Small Systems

The Coalition of Small System Operators plans to file comments on the Further Notice of Proposed Rulemaking to be released by the Commission with respect to cost-of-service procedures. Therefore, we will not address cost-of-service procedures here, except to state that a streamlined form of cost-of-service analysis will serve as the third level of the rate analysis for small systems, following (i) analysis of net income to determine if the system has per se Reasonable Net Income (in which case the system's rates are automatically deemed to be reasonable); and (ii) analysis of rates under the proposed, revised benchmarks, as adjusted for density where appropriate.